No. 17-130

In the Supreme Court of the United States

RAYMOND J. LUCIA, ET AL., PETITIONERS

v.

SECURITIES AND EXCHANGE COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE RESPONDENT

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QUESTION PRESENTED

Whether the Securities and Exchange Commission's use of administrative law judges as hearing officers in administrative proceedings violates constitutional limitations on "Officers of the United States." U.S. Const. Art. II, § 2, Cl. 2.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 3a-36a) is reported at 832 F.3d 277. The order of the en banc court of appeals denying the petition for review by an equally divided court (Pet. App. 1a-2a) is reported at 868 F.3d 1021. The opinion and order of the Securities and Exchange Commission (Pet. App. 37a-109a) are reported at 112 SEC Docket 1754, and are available at 2015 WL 5172953.

JURISDICTION

The judgment of the court of appeals was entered on August 9, 2016. The court granted rehearing and entered a new judgment denying the petition for review on June 26, 2017 (Pet. App. 1a-2a). The petition for a writ of certiorari was filed on July 21, 2017. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Congress has created a comprehensive scheme for the commencement, adjudication, and judicial review of proceedings brought by the Securities and Exchange Commission (SEC or Commission) to enforce the Nation's securities laws. The Commission is authorized under the Securities Act of 1933, 15 U.S.C. 77a *et seq.*, the Securities Exchange Act of 1934, 15 U.S.C. 78a *et seq.*, the Investment Company Act of 1940, 15 U.S.C. 80a-1 *et seq.*, and the Investment Advisers Act of 1940, 15 U.S.C. 80b-1 *et seq.*, to address statutory violations by instituting administrative proceedings before the agency. See, *e.g.*, 15 U.S.C. 77h-1, 78u-3, 80a-9(b), 80a-41(a), 80b-3(e), (f), and (k); 15 U.S.C. 78d, 78*o* (2012 & Supp. IV 2016).

In an administrative enforcement proceeding, the Commission itself may preside and issue a final decision. 17 C.F.R. 201.110. In the alternative, Congress has authorized the Commission to delegate "its functions to a division of the Commission, an individual Commissioner, an administrative law judge, or an employee or employee board." 15 U.S.C. 78d-1(a). Exercising this authority, the Commission has provided by rule that it may delegate the initial stages of conducting an enforcement proceeding to a "hearing officer." 17 C.F.R. 201.110. The hearing officer may be an administrative law judge (ALJ), a single Commissioner, multiple Commissioners (short of a quorum of the Commission), or "any other person duly authorized to preside at a hearing." 17 C.F.R. 201.101(a)(5).

The Commission historically has chosen to assign ALJs to act as hearing officers in its proceedings. Under 5 U.S.C. 3105, "[e]ach agency shall appoint as many

administrative law judges as are necessary for proceedings required to be conducted in accordance with sections 556 and 557 of this title," which are provisions governing agency hearings where an adjudication is required by statute to be determined on the record after an opportunity for a hearing. See 5 U.S.C. 553, 556, 557. The Commission currently employs five ALJs, who are hired through a competitive examination process conducted by the Office of Personnel Management (OPM). 5 U.S.C. 1104(a)(2); 5 C.F.R. 930.201.[1] OPM scores the examinations, ranks the candidates, and prepares a list of eligible candidates. See 5 C.F.R. 332.401, 332.402. In appointing ALJs, agencies may select from a top-three list of eligible candidates provided by OPM, 5 U.S.C. 3317(a), 3318(a), or they may select an ALJ who has an existing appointment from the same or a different agency, 5 C.F.R. 2.2(a). The Commission's ALJs are selected by its Chief ALJ, subject to approval by the Commission's Office of Human Resources on the exercise of authority delegated by the Commission. Pet. App. 295a-297a; cf. 15 U.S.C. 78d(b)(1) (Commission's authority to "appoint and compensate officers, attorneys, economists, examiners, and other employees").

In the capacity of a hearing officer in an SEC enforcement proceeding, an ALJ "shall have the authority to do all things necessary and appropriate to discharge his or her duties." 17 C.F.R. 201.111. Among other responsibilities, the ALJ may administer oaths; issue, revoke, quash, or modify subpoenas; receive and rule on the admission of evidence; withhold a party's access to agency documents; and "rul[e] upon all procedural and

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[1] See U.S. OPM, *ALJs by Agency* (Mar. 2017), https://www.opm.gov/services-for-agencies/administrative-law-judges/#url=ALJs-by-Agency.

other motions." 17 C.F.R. 201.111(h); see 17 C.F.R. 201.111(a), (b), and (c), 201.230(a)(1). In response to "[c]ontemptuous conduct" during a proceeding, the ALJ may exclude the contemnor from the hearing or may "[s]ummarily suspend that person from representing others in the proceeding." 17 C.F.R. 201.180(a)(1)(ii). If the ALJ concludes that a filed document "fails to comply" with the Commission's rules or with the ALJ's own orders, the ALJ may "reject" the filing, which "shall not be part of the record." 17 C.F.R. 201.180(b). The ALJ also may, under certain circumstances, deem a party to be "in default" and thus may "determine the proceeding against that party upon consideration of the record * * * , the allegations of which may be deemed to be true." 17 C.F.R. 201.155(a).

Following an administrative hearing, the ALJ must issue an "initial decision" within a specified number of days. 17 C.F.R. 201.360(a)(2). The ALJ's initial decision may be reviewed by the Commission *sua sponte* or at the request of a party or other aggrieved person. 17 C.F.R. 201.410, 201.411(c). If further review is not requested, or if the Commission declines to undertake such review, the ALJ's initial decision "shall, for all purposes, including appeal or review thereof, be deemed the action of the Commission." 15 U.S.C. 78d-1(c); see 17 C.F.R. 201.360(d)(2). When review by the Commission does occur, the Commission may "make any findings or conclusions that in its judgment are proper and on the basis of the record." 17 C.F.R. 201.411(a). The Commission also may remand the case to the ALJ to take additional evidence or may itself take additional evidence. 17 C.F.R. 201.452. The Commission will either issue its own opinion or will issue a "finality order"

stating that the ALJ's initial decision has become final and effective. 17 C.F.R. 201.360(d)(2); see Pet. App. 90a.

A party who is aggrieved by a final order of the Commission may seek judicial review of that order by filing a petition for review directly in a federal court of appeals. See 15 U.S.C. 77i(a), 78y(a)(1), 80a-42(a), 80b-13(a).

2. Petitioners were registered investment advisers who marketed a wealth-management strategy, which they called "Buckets of Money," under which retirement savings were divided among assets of different risk levels (*e.g.*, bonds, fixed annuities, and stocks) and periodically reallocated as those assets changed in value. Pet. App. 38a, 41a, 127a. The Commission instituted administrative proceedings against petitioners based on allegations that petitioners had used misleading slideshow presentations to deceive prospective clients about how the Buckets of Money strategy would have performed under historical market conditions. *Id.* at 41a-51a; see *id.* at 54a-62a (describing effects of alleged misrepresentations). The Commission charged petitioners with violating the Securities Exchange Act, the Investment Advisers Act, and the Investment Company Act. *Id.* at 238a.

a. The Commission assigned the initial stages of the proceeding to an ALJ, who conducted a hearing that lasted nine days. Pet. App. 116a. The ALJ presided over witness testimony and cross-examinations, admitted documentary evidence, and ruled on objections. Pet. 5. In so doing, the ALJ established "the official record" of the administrative proceeding. Pet. App. 117a n.2.

After the hearing, the ALJ issued an initial decision finding that petitioners had made fraudulent misrepresentations related to one of their investment strategies.

Pet. App. 117a. After the Commission directed the ALJ to make additional factual findings with respect to other alleged misrepresentations, *id.* at 118a, the ALJ issued a revised initial decision finding that respondents had willfully and materially misled investors, in violation of the Investment Advisers Act, *id.* at 195a-225a. The decision ordered a variety of sanctions to be imposed on petitioners, including revocation of their registrations as investment advisers; a permanent bar on associating with investment advisers, brokers, or dealers; a cease-and-desist injunction against future violations; and a total of $300,000 in civil monetary penalties. *Id.* at 235a; see *id.* at 225a-233a.

b. On appeal, the Commission conducted "an independent review of the record, except with respect to those findings not challenged on appeal." Pet. App. 40a. The Commission determined that the ALJ had correctly found that petitioners, in marketing their Buckets of Money Strategy, had willfully made fraudulent statements and omissions in violation of the Investment Advisers Act. *Id.* at 66a-86a. The Commission also largely "affirm[ed]," with limited exceptions, "the sanctions imposed below" by the ALJ. *Id.* at 95a; see *id.* at 95a-107a. Commissioners Gallagher and Piwowar dissented with respect to one aspect of the Commission's liability determination. *Id.* at 110a-114a.

Petitioners argued before the Commission that the proceedings against them were unlawful because the ALJ who had conducted the hearing and issued the initial decision was an "Officer[] of the United States" within the meaning of the Appointments Clause, U.S. Const. Art. II, § 2, Cl. 2. See Pet. App. 86a. Petitioners noted that the ALJ had not been appointed, in accordance with that provision, "by the President, the head of

a department, or a court of law." *Id.* at 87a. The Commission rejected petitioners' argument. In the Commission's view, its ALJs were mere employees rather than constitutional officers because they do not exercise "significant authority independent of the [Commission's] supervision." *Id.* at 88a. Among other things, the Commission explained, its ALJs "issue 'initial decisions' that are * * * not final," *id.* at 88a-89a; a person aggrieved by an initial decision may seek review before the Commission, which "grant[s] virtually all petitions for review," *id.* at 89a (citation omitted); the Commission may review any ALJ decision *sua sponte*, *ibid.*; review of an ALJ's decision is *de novo*, *id.* at 90a-91a; and under the Commission's rules, "no initial decision becomes final simply on the lapse of time by operation of law," but instead becomes final only upon "the Commission's issuance of a finality order," *id.* at 90a (citation and internal quotation marks omitted). The Commission also distinguished this Court's decision in *Freytag* v. *Commissioner*, 501 U.S. 868 (1991), in which special trial judges of the Tax Court were determined to be inferior officers under the Appointments Clause. Pet. App. 92a-93a; see *id.* at 92a ("*Freytag* [is] inapposite here.").

3. On appeal of the Commission's order, a panel of the court of appeals denied the petition for review. Pet. App. 3a-36a.

The court of appeals first rejected petitioners' Appointments Clause challenge, holding that the Commission's ALJs are mere employees rather than officers under the Clause because they do not exercise "significant authority pursuant to the laws of the United States." Pet. App. 11a (quoting *Buckley* v. *Valeo*, 424 U.S. 1, 126 (1976) (per curiam)); cf. *Buckley*, 424 U.S. at 126 n.162 (employees are "lesser functionaries subordinate

to officers"). For that conclusion, the court rested on its prior decision in *Landry* v. *FDIC*, 204 F.3d 1125, 1133-1134 (D.C. Cir.), cert. denied, 531 U.S. 924 (2000), holding that ALJs of the Federal Deposit Insurance Corporation (FDIC) did not exercise significant authority because they could not issue final decisions on behalf of the agency. Pet. App. 12a. The court determined that an SEC ALJ's initial decision is similarly non-final, and it rejected petitioners' attempts to distinguish *Landry*. *Id.* at 13a-19a; see *id.* at 15a ("Until the Commission determines not to order review * * * , there is no final decision that can 'be deemed the action of the Commission.'") (quoting 15 U.S.C. 78d-1(c)). The court also rejected petitioners' argument that the SEC's ALJs "exercise greater authority than FDIC ALJs in view of differences in the scope of review of the ALJ's decisions." *Id.* at 18a. The court acknowledged that "the Commission may sometimes defer to the credibility determinations of its ALJs," but it concluded that "the Commission's scope of review is no more deferential than that of the FDIC Board." *Id.* at 18a, 19a.

The court of appeals further rejected petitioners' attempt to equate the SEC's ALJs with the special trial judges of the Tax Court who were held to be officers in *Freytag*. In the court of appeals' view, the special trial judges were distinguishable because, as "members of an Article I court," they "could exercise the judicial power of the United States" and "issue final decisions in at least some cases." Pet. App. 11a, 12a. The court of appeals also found special trial judges to be different than SEC ALJs because "the Tax Court in *Freytag* was required to defer to the special trial judge's factual and credibility findings unless they were clearly erroneous."

Id. at 19a (citation and internal quotation marks omitted). The Commission, by contrast, "is not required to adopt the credibility determinations of an ALJ." *Ibid.*

On the merits, the court of appeals determined that substantial evidence supported the Commission's finding that petitioners, acting with the requisite scienter, had made material misstatements and omissions in violation of the Investment Advisers Act. Pet. App. 21a-32a. The court also concluded that the Commission had not abused its discretion in ordering sanctions against petitioners. *Id.* at 33a-36a.

4. Petitioners sought rehearing en banc, which the court of appeals granted on February 16, 2017. Pet. App. 244a-246a. The order granting rehearing en banc vacated the panel's judgment but not its opinion. *Id.* at 245a. The order directed the parties to limit their briefs to two issues: (1) whether "the SEC administrative law judge who handled this case [was] an inferior officer rather than an employee for the purposes of the Appointments Clause"; and (2) whether the court should "overrule *Landry*." *Ibid.* On June 26, 2017, the en banc court issued a per curiam judgment denying the petition for review "by an equally divided court." *Id.* at 1a-2a.

DISCUSSION

As this Court has previously observed, the question "[w]hether administrative law judges are necessarily 'Officers of the United States' is disputed." *Free Enterprise Fund* v. *Public Co. Accounting Oversight Bd.*, 561 U.S. 477, 507 n.10 (2010) (quoting U.S. Const. Art. II, § 2, Cl. 2). In prior stages of this case, the government argued that the Commission's ALJs are mere employees rather than "Officers" within the meaning of the Appointments Clause. Upon further consideration, and in light of the implications for the exercise of executive

power under Article II, the government is now of the view that such ALJs are officers because they exercise "significant authority pursuant to the laws of the United States." *Buckley* v. *Valeo*, 424 U.S. 1, 126 (1976) (per curiam).

This Court's review is warranted. The courts of appeals are divided over whether the Commission's ALJs are officers. That division reflects pervasive uncertainty over the scope of this Court's holding in *Freytag* v. *Commissioner*, 501 U.S. 868 (1991), the only decision of this Court since *Buckley* to address the line between employees and officers under the Appointments Clause. The question presented has arisen frequently across the courts of appeals on petitions for review of the Commission's decisions, and it will continue to arise absent this Court's intervention. The question is also extremely important because it affects not merely the Commission's enforcement of the federal securities laws, but also the conduct of adversarial administrative proceedings in other agencies within the government. The petition for a writ of certiorari therefore should be granted, and this Court should appoint an amicus curiae to defend the judgment below.

A. The Commission's ALJs Are Officers Of The United States Rather Than Employees

1. The Constitution vests "[t]he executive Power" of the United States in the President, U.S. Const. Art. II, § 1, Cl. 1, who is charged with responsibility to "take Care that the Laws be faithfully executed," *id.* § 3. The Framers, however, recognized that, "in a republican government," the President would need to rely on the assistance of subordinate officials "to give dignity, strength, purity, and energy to the administration of

the laws." 3 Joseph Story, *Commentaries on the Constitution of the United States* § 1524, at 376 (1833). The Constitution accordingly authorizes the "establish[ment] by Law" of additional executive "Offices," and provides for them to be filled by "Officers of the United States." U.S. Const. Art. II, § 2, Cls. 1, 2; see William Rawle, *A View of the Constitution of the United States of America* 151, 152 (photo. reprint 2003) (2d ed. 1829) (describing the creation of "[s]ubordinate offices" as being "[a]mong the means provided to enable the president to perform his public duties").

The Appointments Clause sets out the exclusive method for appointment of all such Executive Branch officers whose appointments are not otherwise provided for in the Constitution. "[P]rincipal Officer[s]" are appointed by the President, by and with the advice and consent of the Senate; the same method applies to "inferior Officers," except where their appointments have instead been vested by law "in the President alone, in the Courts of Law, or in the Heads of Departments." U.S. Const. Art. II, § 2, Cls. 1, 2; see *United States* v. *Germaine*, 99 U.S. 508, 510 (1879) ("[A]ll persons who can be said to hold an office under the government about to be established under the Constitution were intended to be included within one or the other of these modes of appointment."). The requirements of the Appointments Clause are "among the significant structural safeguards of the constitutional scheme" and are "designed to preserve political accountability relative to important Government assignments." *Edmond* v. *United States*, 520 U.S. 651, 659, 663 (1997).

In *Buckley*, *supra*, the Court explained that "the term 'Officers of the United States' as used in Art. II"

includes all those who hold a position "under the government" and "exercis[e] significant authority pursuant to the laws of the United States." 424 U.S. at 125-126 (citations and internal quotation marks omitted). That description reflects the common understanding at the time of the Founding that "[a] public office is the right, authority and duty, created and conferred by law, by which for a given period * * * an individual is invested with some portion of the sovereign functions of government, to be exercised by him for the benefit of the public." Floyd R. Mechem, *A Treatise on the Law of Public Offices and Officers* § 1, at 1-2 (1890) (summarizing English and early American sources); see 2 Giles Jacob, *The Law-Dictionary*, Tit. "Office" (1797) ("[I]t is a rule, that where one man hath to do with another's affairs against his will, and without his leave, that this is an Office, and he who is in it is an officer."); see also 20 Op. O.L.C. 124, 178-187 (1996).[2]

2. Since *Buckley*, this Court has only once addressed the line between constitutional officers and

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[2] Early decisions of this Court addressing the Appointments Clause were primarily concerned with the question whether Congress *intended* to treat a position it had created by statute as an "office," not whether the functions of the position were required to be performed by an officer appointed pursuant to the Appointments Clause. See, *e.g.*, *Germaine*, 99 U.S. at 509 (civil surgeon could not be prosecuted under criminal statute applicable only to an "officer of the United States who is guilty of extortion") (citation omitted); *United States* v. *Hartwell*, 73 U.S. (6 Wall.) 385, 391-392 (1867) (statute forbidding embezzlement by "officers" applied to clerk appointed by the assistant treasurer in Boston with the approbation of the Acting Secretary of the Treasury) (discussed in *Germaine*, 99 U.S. at 511). In those cases, the Court looked at whether the appointment had occurred in the manner contemplated by the Clause as evidence for whether Congress intended to treat the appointee as an officer.

mere employees. In *Freytag*, *supra*, the Court considered whether certain Tax Court proceedings could be assigned, "for [a] hearing and the preparation of proposed findings and written opinion," to a special trial judge appointed by the Chief Judge of the Tax Court. 501 U.S. at 877. The petitioners in *Freytag* were taxpayers who had objected to tax deficiencies assessed against them and sought review in the Tax Court. *Id.* at 870-871. The proceedings were initially assigned to a special trial judge, who issued "written findings and an opinion" concluding that the petitioners owed additional taxes. *Id.* at 871-872. After unsuccessfully appealing that ruling to the Chief Judge, the petitioners "contended that the assignment of cases as complex as theirs to a special trial judge * * * violated the Appointments Clause of the Constitution." *Id.* at 872.

In addressing that claim, this Court at the outset considered whether "special trial judges may be deemed employees * * * because they lack authority to enter a final decision." *Freytag*, 501 U.S. at 881. That argument, the Court explained, "ignores the significance of the duties and discretion that special trial judges possess." *Ibid.* Unlike special masters, who are hired "on a temporary, episodic basis" to perform ad hoc tasks, special trial judges occupy an office "'established by Law,'" and the "duties, salary, and means of appointment for that office are specified by statute." *Ibid.* (quoting U.S. Const. Art. II, § 2, Cl. 2). The Court placed particular emphasis on the fact that special trial judges, in presiding over preliminary proceedings, "take testimony, conduct trials, rule on the admissibility of evidence, and have the power to enforce compliance with discovery orders." *Id.* at 881-882. "In the course of car-

rying out these important functions," the Court explained, "special trial judges exercise significant discretion." *Id.* at 882.

The Court went on to hold that special trial judges would qualify as constitutional officers "[e]ven if" their ability to issue initial decisions in cases like petitioners' were not so "significant." *Freytag*, 501 U.S. at 882; *ibid.* ("[O]ur conclusion would be unchanged."). That is because, the Court explained, special trial judges are also authorized by law to "render the decisions of the Tax Court [*i.e.*, final decisions] in declaratory judgment proceedings and limited-amount tax cases." *Ibid.* Since it was not disputed that "a special trial judge is an inferior officer for purposes of" those proceedings, the Court concluded, their appointments must comply with the Appointments Clause for all purposes. *Ibid.* ("Special trial judges are not inferior officers for purposes of some of their duties * * * but mere employees with respect to other responsibilities."). Finally, having determined that the Appointments Clause applied to special trial judges, the Court held that their selection could properly be vested under that Clause in the Chief Judge of the Tax Court. *Id.* at 882-892.

Freytag demonstrates that the Commission's ALJs are "inferior officers" rather than "mere employees." 501 U.S. at 882. Like the special trial judges at issue there, the office of an SEC ALJ is characterized by significant "duties and discretion." *Id.* at 881. The position and its compensation have been established by law, see 5 U.S.C. 3105 (appointment authority), 5372(b) (compensation), and the Commission's ALJs have been entrusted with governmental authority "delegate[d]" from the Commission itself, 15 U.S.C. 78d-1(a). ALJs are authorized, among other things, to administer

oaths, hold hearings, take testimony and admit evidence, issue or quash subpoenas, rule on motions, impose sanctions on contemptuous hearing participants, reject deficient filings, and enter default judgments. See 17 C.F.R. 201.111(a), (b), (c), and (h), 201.180(a) and (b).[3] At the conclusion of a hearing, the ALJ issues an "initial decision" that "include[s] findings and conclusions * * * as to all the material issues of fact, law or discretion presented on the record and the appropriate order, sanction, relief, or denial thereof." 17 C.F.R. 201.360(b). If further review of the ALJ's decision is not sought, or a request for such review is denied by the Commission, the ALJ's initial decision "shall, for all purposes, including appeal or review thereof, be deemed the action of the Commission." 15 U.S.C. 78d-1(c); see 17 C.F.R. 201.360(d)(2). In discharging these responsibilities, an ALJ "exercise[s] significant discretion." *Freytag*, 501 U.S. at 881-882. The ALJ is thus an "Officer[ ]" within the meaning of the Appointments Clause.

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[3] The special trial judges at issue in *Freytag* were authorized to "punish contempts by fine or imprisonment." 501 U.S. at 891 (citing 26 U.S.C. 7456(c)). The Commission's ALJs, by contrast, have the arguably less significant authority to punish "[c]ontemptuous conduct" either by "[e]xclud[ing]" the contemnor from the deposition or hearing or by "[s]ummarily suspend[ing] that person from representing others in the proceeding." 17 C.F.R. 201.180(a)(1). The Court's decision in *Freytag*, however, did not identify the power to fine or imprison as evidence of "the significance of the duties and discretion that special trial judges possess." 501 U.S. at 881. Rather, the contempt power was cited only as support for the Court's conclusion that the Tax Court was a "'Court of Law' within the meaning of the Appointments Clause." *Id.* at 890 (brackets omitted); see *id.* at 890-891.

3. In ruling that the Commission's ALJs are not officers, the court of appeals gave dispositive weight to its perception that those ALJs have no authority to issue final decisions that "bind third parties, or the government itself, for the public benefit." Pet. App. 12a-13a; see *id.* at 13a ("Our analysis begins, and ends, there."). The court relied for that conclusion on its prior decision in *Landry* v. *FDIC*, 204 F.3d 1125 (D.C. Cir.), cert. denied, 531 U.S. 924 (2000), where the court read *Freytag* as treating final decision-making authority as the *sine qua non* of officer status. Pet. App. 11a-13a; see *id.* at 12a ("This court understood that it 'was critical to the Court's decision' in *Freytag* that the special trial judge had authority to issue final decisions in at least some cases.") (quoting *Landry*, 204 F.3d at 1134). The Commission's ALJs, the court of appeals asserted, cannot issue final decisions: An ALJ's initial decision "becomes final when, and only when, the Commission issues [a] finality order, and not before then." *Id.* at 15a; see *ibid.* ("[T]he Commission has retained full decision-making powers, and the mere passage of time is not enough to establish finality."). As a result, the court concluded, the "initial decisions are no more final than the recommended decisions issued by FDIC ALJs" that the court had upheld in *Landry*. *Id.* at 17a.

As petitioners here explain (Pet. 20-22), however, the court of appeals erred in placing conclusive weight on the lack of final decision-making authority by the Commission's ALJs. Although *Landry* treated that factor as "critical," 204 F.3d at 1134, *Freytag* held that special trial judges—in light of "the significance of the duties and discretion that [they] possess"—are properly considered officers under the Appointments Clause *despite*

their "lack [of] authority to enter a final decision" regarding tax-deficiency claims. 501 U.S. at 881. To be sure, the Court went on to say that special trial judges would be officers "[e]ven if" their authority over such cases were less "significant," given their authority to render final decisions in other types of cases. *Id.* at 882. But "the Court clearly designated [that statement] as an alternative holding." *Landry*, 204 F.3d at 1142 (Randolph, J., concurring in part and concurring in the judgment). The Court in *Freytag* thus indicated that final authority to make certain discretionary decisions may be sufficient, but is not necessary, to render an official an "Officer[] of the United States" within the meaning of the Appointments Clause.

In attempting to distinguish *Freytag*, the court of appeals further emphasized the relatively low level of deference afforded by the Commission to ALJ decisions. The Commission "reviews an ALJ's decision *de novo* and 'may affirm, reverse, modify, or set aside' the initial decision, 'in whole or in part,' and it 'may make any findings or conclusions that in its judgment are proper and on the basis of the record.'" Pet. App. 18a-19a (quoting 17 C.F.R. 201.411(a)) (brackets omitted). And while the Commission has chosen, as a matter of practice, to "defer to credibility determinations where the record provides no basis for disturbing the finding," the Commission is "not required to adopt the credibility determinations of an ALJ." *Id.* at 19a. By contrast, the court of appeals emphasized, "the Tax Court in *Freytag* was required to defer to the special trial judge's factual and credibility findings unless they were clearly erroneous." *Ibid.* (citation and internal quotation marks omitted).

The court of appeals' proposed distinction from *Freytag* is not persuasive. The level of deference afforded to the decisions of special trial judges played no role in the Court's conclusion that they qualified as "Officers" within the meaning of the Appointments Clause. See 501 U.S. at 880-882. The Court mentioned deference in a different portion of *Freytag* addressing the petitioners' statutory-construction argument, and even there the Court stated that the "point [wa]s not relevant." *Id.* at 874 n.3. Nor, in this case, does the Commission's relative lack of deference to the decisions of its ALJs call into question that such ALJs are "Officers of the United States" under the Appointments Clause. Finally, there is no merit to the court of appeals' attempt to distinguish *Freytag* on the ground that special trial judges were "members of an Article I court [who] could exercise the judicial power of the United States." Pet. App. 11a. In determining that the special trial judges were officers, *Freytag* did not even mention their status as judicial officials.

B. The ALJs' Status As Officers Has Implications For Both Their Selection And Removal That The Court Should Address

The conclusion that ALJs are "Officers of the United States" has important implications under the Constitution regarding the permissible method of their appointment and the manner in which they may be removed from office. This Court's guidance on both issues is accordingly necessary to enable the United States to assess the status of ALJs in various roles across the government and to consider whether the rules governing the selection and removal of those officials comport with constitutional requirements.

1. Under the Appointments Clause, Congress may "vest the Appointment of such inferior Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments." U.S. Const. Art. II, § 2, Cl. 2. The appointment of the ALJ who presided in petitioners' case did not conform to that command. That ALJ was selected by the Commission's Chief ALJ, subject to approval by the Commission's Office of Human Resources. See pp. 2-3, *supra*. The Commission itself, as the constitutional "Head[] of Department[]," did not play any role in the selection. See Pet. App. 295a-297a.

2. Because "Article II confers on the President 'the general administrative control of those executing the laws,' * * * the President therefore must have some 'power of removing those for whom he can not continue to be responsible.'" *Free Enterprise Fund*, 561 U.S. at 492-493 (quoting *Myers* v. *United States*, 272 U.S. 52, 117, 164 (1926)). This Court has accordingly recognized that the Constitution forbids Congress from placing certain restrictions on the power to remove officers of the United States. In *Free Enterprise Fund*, the Court invalidated a statutory scheme that provided for two levels of protection against presidential removal authority: Members of the Public Company Accounting Oversight Board (PCAOB) could be removed by the SEC only for certain limited forms of wrongdoing, see 15 U.S.C. 7217(d)(3), and the Court assumed that the SEC's Commissioners could themselves be removed only for "inefficiency, neglect of duty, or malfeasance in office," 561 U.S. at 487 (citation omitted). The Court determined that the combined effect of those restrictions, which resulted in the PCAOB's exercise of executive authority without any meaningful presidential oversight,

had caused a constitutionally impermissible "diffusion of accountability." *Id.* at 497; see *id.* at 495-508.

Here, the statutory scheme provides for at least two, and potentially three, levels of protection against presidential removal authority: The Commission's ALJs may be removed by the Commission "only for good cause established and determined by the Merit Systems Protection Board," 5 U.S.C. 7521(a), and members of that Board in turn "may be removed by the President only for inefficiency, neglect of duty, or malfeasance in office," 5 U.S.C. 1202(d). And the Commissioners likewise may be insulated from removal (as the Court assumed in *Free Enterprise Fund*), although the Securities Exchange Act is silent on the question. 15 U.S.C. 78d(a). Under *Free Enterprise Fund* and other decisions, the status of the Commission's ALJs as constitutional "Officers" therefore has implications for whether the statutory restrictions on their removal are consistent with separation-of-powers principles.

Petitioners assert (Pet. 34) that the issue of removal authority should be of no immediate concern to the Court because they have not directly challenged the removal restrictions on the ALJ who presided at their hearing. But petitioners do not dispute that the question whether the Commission's ALJs are impermissibly insulated from presidential oversight is informed by the conclusion that such ALJs are constitutional officers who exercise significant authority. See *Free Enterprise Fund*, 561 U.S. at 507 n.10 (reserving the question, in part, because "[w]hether administrative law judges are necessarily 'Officers of the United States' is disputed") (citing *Landry*, *supra*). And even if petitioners are successful in obtaining invalidation of the proceedings against them in this case, and further proceedings occur

in front of a properly appointed ALJ, the removal question would continue to cloud the ALJ's authority. Indeed, another litigant has already raised a separation-of-powers challenge to ALJ removal protections alongside an Appointments Clause challenge; that case has been briefed in the D.C. Circuit and is being held pending the disposition of this petition. See 8/8/17 Order, *Timbervest* v. *SEC*, No. 15-1416.

It is critically important that the Court, in considering whether the Commission's ALJs are "Officers of the United States," address whether the restrictions imposed by statute on their removal are consistent with the constitutionally prescribed separation of powers. Addressing that issue now will avoid needlessly prolonging the period of uncertainty and turmoil caused by litigation of these issues. See pp. 24-26, *infra*. If the Court believes that petitioners' framing of the question presented is not broad enough to encompass the issue, the government has reframed the question to leave no doubt on that score. In the alternative, the Court may find it desirable to add a question presented that specifically addresses it. See, *e.g.*, *NLRB* v. *Noel Canning*, 133 S. Ct. 2861 (2013) (directing the parties to brief and argue an additional question, which had not been considered by the courts below). Whatever the appropriate course, the government respectfully submits that addressing both the appointment and removal of the Commission's ALJs will provide needed clarity to agencies and regulated parties, while minimizing what could otherwise be severe disruption to a large number of current and future administrative proceedings.

C. This Case Is The Preferable Vehicle For Resolving The Division Among The Courts Of Appeals

This Court's review is warranted because the question presented has led to significant disagreement in the courts of appeals. That disagreement has generated substantial confusion and disruption for the Commission in its enforcement of the Nation's securities laws, as well as for other federal agencies that use ALJs in administrative proceedings.

1. In the proceeding below, a panel of the D.C. Circuit held that the Commission's ALJs are employees rather than officers. The court subsequently granted rehearing en banc, Pet. App. 244a-246a, and ultimately denied the petition for review by an equally divided vote, *id.* at 1a-2a. Under D.C. Circuit Rule 35(d), an order granting en banc review vacates "the panel's judgment, but ordinarily not its opinion." Consistent with that rule, the court's order granting rehearing en banc vacated only the panel's "judgment," 2/16/17 Order 1, leaving the panel's opinion undisturbed.

The Commission has therefore explained, in other cases raising Appointments Clause challenges, that the panel's opinion in this case remains in effect. See, *e.g.*, Commission Br. at 62, *Gonnella* v. *SEC*, No. 16-3433 (2d Cir. July 17, 2017). The Commission has also urged the D.C. Circuit to hold follow-on cases raising the same question in abeyance pending this Court's disposition of the petition for a writ of certiorari. See, *e.g.*, Mot. to Hold Case in Abeyance, *Timbervest, LLC* v. *SEC*, No. 15-1416 (July 20, 2017). The D.C. Circuit has granted those abeyance motions. See, *e.g.*, 8/8/17 Order, *Timbervest, LLC* v. *SEC*, No. 15-1416.

2. In *Bandimere* v. *SEC*, 844 F.3d 1168 (2016), a divided panel of the Tenth Circuit reached the opposite

conclusion on the question presented under materially identical circumstances. There, an ALJ issued an initial decision finding that the respondent had violated anti-fraud and registration provisions of the federal securities laws by operating as an unregistered broker and by failing to disclose potentially negative facts to investors. *In re David F. Bandimere*, Securities Act Release No. 9972, 2015 WL 6575665, at *1 (Oct. 29, 2015). On review of the ALJ's initial decision, the Commission upheld the liability finding and imposed disgorgement and civil-penalty sanctions. *Id.* at *2. The Commission also rejected the respondent's argument that its ALJs are officers under the Appointments Clause. *Id.* at *19-*21.

The Tenth Circuit granted the respondent's petition for review, holding that the Commission's ALJs are invested with powers that require their appointment as inferior officers under the Appointments Clause. *Bandimere*, 844 F.3d at 1179-1182. In reaching that conclusion, the court relied on *Freytag*, which it interpreted as turning on the significance of the special trial judges' duties, not on their authority to render final decisions of the Tax Court. *Id.* at 1182-1185; see *id.* at 1179 (The Commission's ALJs "exercise significant discretion in performing 'important functions' commensurate with the [special trial judges'] functions described in *Freytag*.") (quoting 501 U.S. at 882). The court thus expressly "disagree[d]" with the D.C. Circuit's decisions in *Landry* and in this case, which, the Tenth Circuit determined, had "place[d] undue weight on final decision-making authority." *Id.* at 1182.

Judge McKay dissented, arguing that *Freytag* does not "mandate[] the result proposed here." *Bandimere*, 844 F.3d at 1194. Like the panel in this case, Judge

McKay distinguished the special trial judges at issue in *Freytag* because of their authority to enter final decisions in a number of cases and because "the Tax Court was required to defer to its special trial judges' findings." *Id.* at 1197. Judge McKay emphasized that the Commission's ALJs, by contrast, "possess only a 'purely recommendatory power.'" *Ibid.* (quoting *Landry*, 204 F.3d at 1132). In May 2017, the Tenth Circuit denied the Commission's petition for rehearing en banc, with Judges Lucero and Moritz dissenting. See *Bandimere* v. *SEC*, 855 F.3d 1128, 1128-1133.

On September 29, 2017, the government filed a petition for a writ of certiorari in *SEC* v. *Bandimere*, No. 17-475, urging this Court to resolve the question whether the Commission's ALJs are inferior officers rather than employees. But the government explained that this case, rather than *Bandimere*, presents the Court with the preferable vehicle for addressing that question. See Pet. at 9, *Bandimere*, *supra* (No. 17-475). The government accordingly "respectfully request[ed] that the Court hold th[e] petition" in *Bandimere* "pending its consideration of the petition" in this case. *Ibid.*

3. The disagreement in the courts of appeals has significant implications for the Commission's ability to discharge its statutory responsibilities. Congress has granted the Commission broad authority to conduct administrative enforcement proceedings to determine whether the securities laws have been violated and, if so, what remedies are appropriate. See 15 U.S.C. 77h-1, 78u-3; 15 U.S.C. 78d, 78*o* (2012 & Supp. IV 2016). Certain of the Commission's enforcement powers, such as the power to revoke the registration of a registered security under 15 U.S.C. 78*l*(j), can be exercised *only* through the initiation of an administrative proceeding.

In conducting such proceedings, the Commission historically has assigned an ALJ to preside over the hearing and issue an initial decision, which the Commission then reviews. See 15 U.S.C. 78d-1(a). The abeyance status of cases pending in the D.C. Circuit—which has automatic venue in securities cases, see 15 U.S.C. 77i(a), 78y(a)(1), 80a-42(a), 80b-13(a)—thus means that the Commission's ability to enforce the nation's securities laws has, in significant respects, been put on hold pending this Court's resolution of the question presented. Appointments Clause challenges to the Commission's ALJs have also been raised in several other cases across the courts of appeals, indicating that the gridlock will soon be even more widespread.[4]

4. Finally, the conflict in the courts of appeals on the question presented has created substantial uncertainty for other agencies that employ ALJs in a manner similar to the Commission. A panel of the Fifth Circuit recently granted a stay of an FDIC order, concluding that the respondent had established a likelihood of success on his claim that the ALJ who presided over his proceeding was an officer who was not properly appointed under the Appointments Clause. *Burgess* v. *FDIC*, 871 F.3d 297 (2017). In so ruling, the court expressly disagreed with the D.C. Circuit's decision in *Landry*. *Id.* at 301 ("We therefore conclude, contrary to the D.C. Circuit's decision in *Landry*, that final decision-making authority is not a necessary condition for Officer sta-

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[4] See, *e.g.*, *Gonnella* v. *SEC*, No. 16-3433 (2d Cir. filed Oct. 7, 2016); *Bennett* v. *SEC*, No. 16-3827 (8th Cir. argued June 7, 2017); *J.S. Oliver Capital Mgmt., L.P.* v. *SEC*, No. 16-72703 (9th Cir. filed Aug. 15, 2016); *Feathers* v. *SEC*, No. 15-70102 (9th Cir. filed Jan. 9, 2015).

tus."). Given the frequency with which ALJs are employed in administrative proceedings by a variety of federal agencies, see, *e.g.*, 7 C.F.R. 1.144, 1.411(f) (Department of Agriculture); 12 C.F.R. 1081.103 (Consumer Financial Protection Bureau); 18 C.F.R. 385.102(e), 385.708 (Federal Energy Regulatory Commission); 29 C.F.R. 102.35 (National Labor Relations Board); 40 C.F.R. 22.3(a), 22.4(c) (Environmental Protection Agency), this Court's resolution of the question presented is necessary to prevent the same disruption that has affected the Commission's proceedings from spreading throughout the government.

CONCLUSION

The petition for a writ of certiorari should be granted. If appropriate, the Court should reframe the question presented or add a question presented to address the issue of removal.

Respectfully submitted.

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